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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

COMMISSIONERS

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JEFF HATCH-MILLER, Chairman
WILLIAM A. MUNDELL
MARC SPITZER
MIKE GLEASON
KRISTIN K. MAYES

DOCKETED BY

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AZ Corporation Commission
Director Of Utilities

IN THE MATTER OF APPLICATION OF
MONTEZUMA ESTATES PROPERTY OWNERS'
ASSOCIATION dba MONTEZUMA ESTATES
WATER COMPANY FOR APPROVAL OF THE
SALE OF ASSETS AND TRANSFER OF ITS
CERTIFICATE OF CONVENIENCE AND
NECESSITY.

DOCKET NO. W-02064A-04-0270
DOCKET NO. W-04254A-04-0270

DECISION NO. 67583

OPINION AND ORDER

DATE OF HEARING:

July 8 and October 28, 2004

PLACE OF HEARING:

Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE:

Marc E. Stern

APPEARANCES:

Mr. Douglas Fitzpatrick, on behalf of
Montezuma Estates Property Owners
Association dba Montezuma Estates Water
Company;

Richard Rink, Intervenor; pro se

Owen L. Cotton, Intervenor, pro se; and

Mr. David M. Ronald, Staff Attorney, Legal
Division, on behalf of the Utilities Division of
the Arizona Corporation Commission.

BY THE COMMISSION:

On April 9, 2004, Montezuma Estates Property Owners Association (MEPOA") dba Montezuma Estates Water Company ("Applicant" or "Company") filed with the Arizona Corporation Commission ("Commission") an application requesting the Commission's approval for the sale of its water utility assets and transfer of its Certificate of Convenience and Necessity ("Certificate") to Montezuma Rimrock Water Company, L.L.C. ("MRWC").

On May 12, 2004, by Procedural Order, pursuant to A.R.S. 41-1074(C), the application herein was deemed administratively complete and in accordance with A.A.C. R14-3-101, the Commission scheduled a hearing to commence on July 8, 2004.

1 On June 8, 2004, Applicant filed certification that notice had been provided pursuant to the
2 Commission's Procedural Order.

3 On June 14, 2004, Richard Rink, a property owner in the Company's certificated service area,
4 filed a request to intervene.

5 On June 24, 2004, by Procedural Order, Mr. Rink's request to intervene was granted without
6 objection, and the Commission's Utilities Division ("Staff") filed its Staff Report.

7 On July 1, 2004, Applicant filed its response to the Staff Report.

8 On July 8, 2004, a full public hearing was convened before a duly authorized Administrative
9 Law Judge of the Commission at its offices in Phoenix, Arizona. Applicant and Staff appeared with
10 counsel. Ms. Patricia Arias, the manager and sole member of MRWC, appeared on her own behalf.
11 Mr. Rink appeared on his own behalf. Mr. Owen L. Cotton, a member of a limited liability company
12 which owns vacant and rental properties in the Company's certificated service area, appeared and
13 provided a copy of a letter dated June 18, 2004, which he had mailed to the Commission requesting
14 intervention. Mr. Cotton acknowledged that he had not sent a copy of his request to any other party,
15 Docket Control or the Hearing Division. Without objection, his request for intervention was granted
16 at the outset of the proceeding. Based on the record, the timeclock rule was suspended following the
17 request by Applicant for at least a 90-day continuance to resolve certain issues raised in the hearing
18 and it was agreed that the Company would file a motion to reschedule the proceeding for the taking
19 of additional evidence.

20 On August 12, 2004, Staff filed a Status Report and a late-filed exhibit.

21 On September 1, 2004, Applicant filed a Motion to Reset the Hearing.

22 On September 13, 2004, by Procedural Order, an additional hearing was scheduled on the
23 application.

24 On October 28, 2004, the hearing was reconvened at the offices of the Commission in
25 Phoenix, Arizona. The Company and Staff appeared with counsel. Ms. Arias appeared on her own
26 behalf as the sole member of MRWC. Mr. Rink and Mr. Cotton, the Intervenors, appeared on their
27 own behalf. At the conclusion of the hearing, the matter was taken under advisement pending
28 submission of a Recommended Opinion and Order to the Commission.

* * * * *

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

FINDINGS OF FACT

1. Pursuant to the authority granted by the Commission in Decision No. 52468 (September 18, 1981), the Company, a non-profit homeowners association, provides public water utility service to an area in various parts of Yavapai County, in the vicinity of Maguireville, Arizona.

2. Applicant is presently operated by its homeowners association and provides public water utility service to approximately 120 customers.

3. The Company has been managed by MEPOA's president for the past six years. He owns approximately 15 lots in the Applicant's certificated service area, which contains approximately 700 lots owned by approximately 550 different owners.¹

4. Several times during the proceeding, Mr. Sanchez described the general lack of interest, apathy and indifference displayed by customers and/or lot owners in the Company's certificated service area in the operation of the Company. He testified that only 38 of the 550 lot owners pay their annual \$25 assessment to MEPOA and are in so-called "good standing" entitling them to vote at association meetings as set forth in the MEPOA By-Laws.

5. On April 9, 2004, the Company filed an application requesting the Commission's authorization for the sale of its assets and transfer of its Certificate to MRWC which will then operate the utility which supplies water to the Company's certificated service area. MRWC is a limited liability company whose only member is Ms. Patricia D. Arias, Mr. Sanchez' daughter.

6. Ms. Arias has been the Company's certified operator for approximately two and one-half years and will continue in this capacity after the acquisition. She reads the Company's meters for billing purposes and also takes water samples for testing purposes.² Maintenance on the system is performed by outside contractors or volunteers directed by Mr. Sanchez.

¹ According to Mr. Peter Sanchez, the president of the homeowners association, the certified area is an old subdivision developed by a convicted fraudulent land developer, Ned Warren. Apparently, some of the lots are located in a flood plain and are unfit for construction, and are being condemned by Yavapai County.

² Ms. Arias is presently employed on a full-time basis by the Arizona Department of Environmental Quality ("ADEQ") as an environmental health specialist.

1 7. On June 8, 2004, Applicant filed certification that notice of the proposed sale of assets
2 and transfer of Certificate had been mailed to its customers. In response thereto, no protests were
3 received, but Mr. Rink and Mr. Cotton requested and were granted intervention because they own
4 property in Applicant's certified service area although neither of the intervenors is a customer of the
5 Company.

6 8. Mr. Rink, who owns approximately five vacant lots in the Company's service area,
7 does not pay the \$25 annual assessment and is not a member in "good standing" in MEPOA. Mr.
8 Cotton is a member in "good standing" and is a partner in a rental triplex whose residents are
9 customers of the Company. He also owns several other undeveloped lots in the certified area.

10 9. Applicant has obligations due for refunds and MRWC will continue to meet the refund
11 and/or deposit obligations due the Company's existing customers.

12 10. MRWC will continue to charge the rates and charges previously authorized for the
13 Company by the Commission.

14 11. The Company does not have a county franchise because all roads in the certificated
15 service area are owned and maintained by MEPOA.

16 12. Applicant is current on Commission filings and is current on the payment of its sales
17 and property taxes.

18 13. Although a formal purchase agreement had not been completed at the time of the
19 initial hearing, Mr. Sanchez, on behalf of the Company, had entered into an agreement in principle to
20 sell the Applicant's assets and transfer its Certificate to MRWC. Ms. Arias agreed to pay MEPOA
21 \$100,000 for the system. Initially, she had planned to pay \$20,000 in cash and to finance the
22 remaining \$80,000 with a bank loan secured by the Company's assets. However, she subsequently
23 entered into a written sales agreement with MEPOA whereby MRWC will pay the entire purchase
24 price of \$100,000 in cash. A copy of the agreement in the form of escrow instructions was
25 subsequently filed in the Docket.

26 14. Prior to entering into the sales agreement, the Company's board agreed to its sale after
27 a vote by the lot owners including the 38 members in "good standing". Of the approximately 550
28 property owners who were sent ballots to approve the sale, only 110 responses were received with

1 only 11 "no" votes. Of the "no" votes, only three members in "good standing" voted "no", one of
2 whom was Mr. Cotton.

3 15. Mr. Sanchez indicated that while there are 147 residences in the Company's certified
4 area, only approximately 120 residences are served by the Company. The ranks of the customers
5 grow by approximately 20 new connections a year. The remaining residents who reside in the service
6 area either have their own wells or haul water.

7 16. Although the Company previously experienced excessive water loss, it has solved this
8 problem and now experiences only minimal water loss.

9 17. Although Applicant has two well sites, it is primarily making use of its largest well
10 because of a drop in the water table which may partially be due to the demand for water by the
11 adjacent 600 acre subdivision, Thunder Ridge. In the interim, the Company is negotiating for a third
12 well site.

13 18. To provide service, the Company has two well sites, two 10,000 gallon storage tanks
14 and two 2,000 gallon pressure tanks. The primary well used by the Company for water service
15 pumps 35 gallons of water per minute ("gpm"). Applicant's second well pumps approximately 11
16 gpm, but is not used presently.

17 19. Mr. Sanchez related that in the past, Arizona Water Company ("AWC"), which
18 provides water service to Thunder Ridge through its Rimrock System, had been contacted to purchase
19 the Company, but AWC had declined the Company's offer to sell in 1999.

20 20. According to Mr. Sanchez, the Company is breaking even and uses its Commission-
21 approved \$1,200 hook-up fee to add back bone plant and make other improvements. However, much
22 of the operational work is done by MEPOA volunteers.

23 21. The association's board plans to divide the proceeds from the sale of assets equally
24 between all of the lot owners if the application is approved by the Commission and the sale goes
25 forward.

26 22. Although Mr. Rink does not pay his annual assessment, and comply with MEPOA's
27 By Laws, he stated that he supports the sale and transfer. However, Mr. Rink believes the board of
28 MEPOA is not following state law for a number of reasons including its failure to adopt a clear

1 procedure for the cancellation of MEPOA membership due to the nonpayment of the annual
2 assessment, but he has not pursued legal action against the association.

3 23. During the initial hearing, Mr. Cotton testified that he had spoken with an official of
4 AWC and believes that AWC is interested in taking another look at the system. He believes that
5 AWC would be a better financial choice as a buyer and would protect his interests as an investor in
6 lots in the certified area.

7 24. Staff, at the first hearing, recommended the denial of the application and maintained
8 this position at the conclusion of the proceeding. Staff raised concerns that the purchase price could
9 be far in excess of Applicant's fair value rate base ("FVRB") found in its last rate case resulting in
10 Decision No. 64665 (March 25, 2002).³

11 25. After the conclusion of the initial proceeding herein, Staff was contacted by AWC by
12 letter and was advised that AWC is interested in the acquisition of the Company if the Company
13 wishes to pursue the matter with AWC. However, AWC did not seek intervention in the proceeding
14 nor pursue the matter further.⁴

15 26. According to Mr. Sanchez, after the initial hearing, the board of MEPOA met with
16 members/customers who indicated that they did not want the sale of assets to proceed with AWC.
17 After the customer meeting and during the second hearing, Mr. Sanchez testified concerning the
18 possibility of the sale of the water utility to AWC as follows:

19
20 I've held one meeting here just recently, and it was because the
21 judge here, Judge Stern, requested that we have a meeting so that we could
22 get the opinion of the members. We didn't have very many members that
showed up at the meeting, but all the members but one said no. One of the
main reasons is because they wanted to stay small. They didn't want to go
to Arizona Water.

23 I also had several telephone calls from several of our members and
24 people that live in our community asking me about what's going on. I've
25 taken the time to explain to them what has been going on, and after I
talked to him, I haven't had a yes. Everybody has voted no.

26 I believe that I've spoken to, right at about 19, 20 of our customers
27 on an individual basis and they don't want us to sell to Arizona Water.

28 ³ The Commission, in Decision No. 64665, found the Company's FVRB to be \$51,044.

⁴ According to Ms. Arias, a representative of AWC indicated to her that it would only offer approximately
\$80,000 for the system.

At that point, as a representative of our community, I took it upon myself to say no to Arizona Water.

27. In support of its acquisition of the Company, MRWC is willing to secure a performance bond.

28. With respect to arsenic, Mr. Sanchez indicated that he believes Applicant's primary well has arsenic content of thirty parts per billion ("ppb") and its second well 70 ppb, well in excess of the new maximum standard of 10 ppb effective January 2006. The Company and Ms. Arias have been exploring a plan to adopt a point of use reverse osmosis ("R.O.") system to meet the new arsenic standard because they believe it will be more cost effective for the Company's customers than the arsenic treatment plan approved for AWC's Rimrock system.

29. Ms. Arias believes that the R.O. point of use system would cost Applicant approximately \$50,000, far less than the \$256,000 based on the ADEQ Master Plan for arsenic reduction and result in lower customer costs.

30. According to the most recent status report of ADEQ dated July 16, 2004, Applicant is providing water which meets ADEQ requirements and meets the standards of the Safe Drinking Water Act.

31. The Company has previously filed a Backflow Prevention Tariff and Curtailment Tariff, both of which were approved by the Commission.

32. Staff is recommending the denial of the Company's application herein because Staff does not believe there is sufficient financial evidence to support MRWC's offer to acquire the Company's assets to insure that the customers will continue to receive equal or better service than from the Applicant, even with the payment for the utility being made all in cash.

33. Staff believes that Applicant's customers could be better served by the transaction going forward with AWC as the buyer for the following reasons: AWC's Rimrock system is within 600 feet of Applicant's system; AWC has a strong financial history; AWC has a new 350 gpm well which can be interconnected with Applicant's system and used to provide service to the Company's service area; and AWC already has a Commission approved plan for arsenic treatment when it is necessary.

34. Staff also recommended that if the Commission approves the purchase of the system

1 by MRWC, some form of performance bond should be imposed to insure ongoing viable operations
2 in the event MRWC encounters financial difficulties.

3 35. When service is requested in an unserved area, the Commission generally prefers that
4 the area be included in the certificated service area of a nearby existing public water utility with a
5 good record of compliance which is willing to supply reliable service at a reasonable cost, as opposed
6 to issuing a new Certificate to a start up utility. This is because the policy supports orderly growth
7 and promotes the expansion and consolidation of small water companies or systems. The
8 Commission has previously found this policy leads to economies of scale in the provision of utility
9 service and is in the best interest of the public rather than promoting numerous small systems with
10 limited opportunities for growth and expansion.⁵

11 36. The application before us differs from the Commission's policy with respect to the
12 start-up utility scenario described above as follows:

- 13 • the transferor is an existing public utility which is owned and operated in a
14 compliant fashion by its homeowners association;
- 15 • Applicant has received no other offers from any other existing public utility to
16 purchase its system and there is evidence that the existing lot owners and/or
17 customers have no desire to be acquired by AWC, the neighboring utility;
- 18 • while noting the concerns of Mr. Rink and Mr. Cotton, a valid offer to
19 purchase the Company has been made by MRWC which is owned by
20 Applicant's certified operator who has been operating the Company in
21 compliance with Arizona law, the Commission's rules and ADEQ's
22 requirements; and
- 23 • there is no evidence that MRWC is not a fit and proper entity to receive the
24 assets and Certificate of the Company.

25 37. We shall approve the application subject to MRWC complying with the following
26 conditions, which include the filing of a performance or surety bond since MRWC has not previously
27 been involved in the operation of a public utility:

- 28 • MRWC shall secure and file, with the Commission, at least 30 days prior to the
close of the transaction, a form of performance or surety bond in the amount of
\$30,000;
- MRWC shall maintain said performance or surety bond until further Order of
the Commission;

⁵ See Decision No. 67277 (October 5, 2004) and Decision No. 66780 (February 13, 2004).

- MRWC shall file, with the Commission, at least 30 days prior to the close of the transaction, certification that any outstanding long-term debt of the Company, if any, will be paid by Applicant from the proceeds of the purchase price and shall not be assumed by MRWC;
- MRWC shall continue to charge the Company's existing rates and charges;
- MRWC shall not encumber the assets of the utility in any way without prior Commission approval;
- MRWC shall maintain its books and records in accordance with the NARUC Uniform System of Accounts;
- MRWC shall file an annual report with the Director of the Utilities Division concerning its hook-up fee account in the form ordered in Decision No. 64665;
- MRWC shall file, with the Commission, within 60 days of the effective date of this Decision, its arsenic treatment plan, if not previously filed by Applicant; and
- MRWC shall not seek recovery of any excess cost over book value paid in this transaction in a future rate proceeding.

CONCLUSIONS OF LAW

1. Applicant is a public service corporation within the meaning of Article XV of the Arizona Constitution and A.R.S. §§ 40-281, 40-282 and 40-285.

2. The Commission has jurisdiction over the Company and of the subject matter of the application.

3. There is a continuing need for the provision of water utility service to the public in the Company's certificated service area.

4. MRWC is a fit and proper entity to receive the assets and Certificate of the Company.

5. Notice of the Company's application as described herein was given in the manner prescribed by law.

6. The conditions as set forth in Findings of Fact No. 37 are reasonable and should be adopted.

ORDER

IT IS THEREFORE ORDERED that the application of Montezuma Estates Property Owners Association for approval of the sale of utility assets and transfer of its Certificate of Convenience and Necessity to Montezuma Rimrock Water Company, L.L.C. is hereby approved.

IT IS FURTHER ORDERED that Montezuma Rimrock Water Company, L.L.C. shall

1 continue to charge water customers the existing rates and charges until further Order by the
2 Commission.

3 IT IS FURTHER ORDERED that the approval of Montezuma Estates Property Owners
4 Association's application for the sale of its assets and transfer of its Certificate of Convenience and
5 Necessity shall be expressly contingent upon Montezuma Rimrock Water Company, L.L.C. filing
6 with Docket Control, at least 30 days prior to the close of this transaction, a copy of a form of
7 performance or surety bond in the amount of \$30,000 to insure that Montezuma Rimrock Water
8 Company, L.L.C. shall meet its obligations arising under its Certificate.

9 IT IS FURTHER ORDERED that Montezuma Rimrock Water Company, L.L.C. shall
10 maintain said performance or surety bond with copies of same to be filed annually with the
11 Commission on the anniversary of the effective date of this Decision until further Order of the
12 Commission.

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1 IT IS FURTHER ORDERED that Montezuma Rimrock Water Company, L.L.C. shall comply
2 in all respects with Findings of Fact No. 37 and Conclusion of Law No. 6 or the approval granted
3 hereinabove shall be null and void.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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8 CHAIRMAN

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11 COMMISSIONER

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14 COMMISSIONER

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17 COMMISSIONER

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20 COMMISSIONER

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23 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
24 Secretary of the Arizona Corporation Commission, have
25 hereunto set my hand and caused the official seal of the
26 Commission to be affixed at the Capitol, in the City of Phoenix,
27 this 15th day of Feb., 2005.

28
BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT Jeffrey M. Hatch-Miller

DISSENT _____

MES:mj

1 SERVICE LIST FOR:

MONTEZUMA ESTATES PROPERTY OWNERS'
ASSOCIATION dba MONTEZUMA ESTATES
WATER COMPANY

3 DOCKET NOS.:

DOCKET NO. W-02064A-04-0270 and
DOCKET NO. W-04254A-04-0270

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7 Rimrock, AZ 86335

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13 Montezuma Rimrock Water Company LLC
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15 Patricia D. Arias
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17 Richard Rink
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